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THE CAPITAL STRUCTURE OF MALAYSIAN FIRMS IN THE AFTERMATH OF ASIAN FINANCIAL CRISIS 1997

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ABSTRACT

The Asian Financial Crisis 1997 had revealed the issues of excessive leverage that caused the firms in Malaysia for being vulnerable to the economic turmoil. Hence, capital structuring and particularly the establishment of the contingent capital structure have been the central concern. Grounded on the contingency theory and the traditional capital structure theories, this study intends to identify what constitutes organizational-environmental fit to the contingent capital structure in Malaysia and how fast they had adjusted towards their contingent capital structure in the aftermath of the crisis. The findings reveal that while Malaysia has successfully sustained the firms' leverage to a lower level, it was not so successful to ensure speedy adjustment given its rigorous institutional settings and also access to financial and capital market. A better understanding of the contingent capital structure formulation and adjustment process via fresh empirical evidence do not only provide insights to the practitioners into the adaptation strategy but also have important implications for the design and implementation of the financial reforms in addressing future crisis.

Field of Research: *Determinants of contingent capital structure, speed of adjustment.*

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1. Introduction

Following the outbreak of the Asian Financial Crisis 1997, several literature have highlighted the issues of excessive leverage that cause the firms in Malaysia for being vulnerable to the economic turmoil (Claessens et al., 2000; Driffield and Pal, 2001, 2010). The issue of overleveraged became crucial as not only the distressed firms were adversely affected but the financial institutions were preoccupied with non-performing loans (NPL).[1] The country then undertook substantial institutional restructuring to remedy the ruins caused by the crisis.[2]

1. Several highly leveraged firms were declared bankruptcy while some were rescued by the government (Ariff et al, 2008). Consequently, the financial institutions' NPL doubled from 4.1% in late 1997 to 9.0% by the end of 1998.
2. The government did not resort from IMF but decided to form a National Economic Action Council (NEAC), a consultative body to the Cabinet. The NEAC established two institutions: Danaharta was set up with the aim of acquiring and managing the non-performing loans from the banking sector while Danamodal was formed to recapitalize ill banks whose capital adequacy had fallen below 9%. Later, the Corporate Debt